CHAPTER – I

INTRODUCTION

1.1 Background of the Study

The development of any country depends upon economic development of the country and economic development is supported by financial infrastructure of the country. Banks play vital role in the economic growth of the country. Every well-organized financial institutions including finance companies, commercial banks, join venture banks and other financial institutions, plays significant, role for the development of the country. They collect scattered financial resources from the mass and invest them among those who are associated with the economic, commercial and social activities of the country. This provides fuel to development process. Integrated and speedy development of the country is possible only when competitive financial service reaches everywhere ion the country. It has been well established fact that the economic activities of any country can hardly be carried forward without the assistance and support of financial institution.

Banks constitute an important segment of financial infrastructure of any country. Banking when properly organized, aids and facilities the growth of trade and industry and enhance national economy. In the modern economy banks are considered as leaders of development. Besides contribution in overall development of the country, the commercial banks render numerous services to their customer in view of facilitating their economic and social life.

Investment is an important ingredient of overall national economic development because it ensures efficient allocation of fund to achieve the materials and economic well being of the society. Investment policy is an important factor of the investment practice. Investment refers to sacrifice of current money for future money, generally two attributes are involved in it, they are time and risk.

In this study, the word investment conceptualized the investment of income, savings or other collected fund. The term investment covers a wide range of activities. It is widely known fact that an investment is only possible where there is adequate savings. If all the incomes and savings are used to fulfill the incomes and savings are used to fulfill the minimum needs, then there is no existence of investment. Thus, both saving and investment are interrelated.

Investment policy is the most important factor of the investment practice. The joint venture commercial banks formulate sound investment policies to make it more effective, which eventually contributes to the economic growth of the country. The sound investment policy helps the banks to maximize the quality and quantity of investment and helps to achieve the loan objective of profit maximization and social welfare. Formulation of sound investment policies and coordinated and planned efforts push forward to the forces of economic growth.

The commercial banks should careful while performing the credit creation function. Investment policy should be formulated in such a way that maximizes the profit and minimizes the risk from lending. Nepalese joint venture commercial banks are far behind fulfilling the responsibility to invest in the crucial sectors of the economy for the upliftment of the national economy. Good investment policy ensures maximum amount of investment to all sectors with proper utilization.

In the present context there is tough competition in the banking market but not enough opportunity to make investment. In this salutation, joint venture banks can take initiation in search of new opportunities to survive in the competitive market and earn satisfactory profit. There is high liquidity in the money market but here seems to be no profitable area to invest. Flow of money is more than requirement. Likewise, the banks and financial companies (institutions) are offering very low deposit interest rate. This indicates that the joint venture banks should be able to create new investment opportunities to make investment to survive and earn maximum profit in the highly competitive market.

For the entire development of the country the proper development of industry and trade in must. Therefore, the banks should give priority for the accelerating the economic growth of the country. As the strong economic condition of a country is represented by the development of industry, trade and business, which is main sector of the banks to carryout its activities and to achieve its aim of profit maximizing. Proper investment practice assists the joint venture banks to make profitable investment which helps in the development of country as well as achieve the objective of making the profit.

1.2 Brief History of the Evaluation of Banking

The evolution of banking had started a long time ago. In ancient Greece, the famous temple of Delphi and Olympia served as the great depositories for people's surplus funds and these were the centers of money lending transactions. However, as a public enterprises banking started around the middle of the twelfth century in Italy. The first bank called the **"Bank of Vanice"** was established in Vanice, Italy in 1157 A.D. Following establishment of this bank two other banks **"Bank of**

Barcelona" and **"The Bank of Geneva"** established in 1609 with the expansion of commercial banking activities in Northern Europe, No. of private banking organization sprang up there and slowly it spread through out the world.

The evaluation of organized financial system has a more recent history in Nepal than in other counties. Like other countries, landlords, moneylenders, merchant, goldsmith etc. are ancient bankers of Nepal. Even though the establishment of banking industry is very recent. Some traditional banking operations were practice even in the ancient time. The establishment of "Tejarath Adda" during the year 1877 A.D. was the first step in institutional development to provide loan of a lower rate against collateral of gold and silver. The area of its functioning was limited in Kathmandu valley and some urban areas of Terai. Tejarath Adda may be regarded as the father of modern banking institutions. The development of trade with different countries increases the necessity of eh institutional banker. Which can act more widely to enhance the trade and commerce and to touch the remote non banking sector in the economy. Taking into consideration this situation the "Ugyog Parishad" was constituted in 1963 A.D. After one year, it formulated the "Company Act" and "Nepal Bank Act" in 1937 A.D. Nepal Bank Limited was established under Nepal Bank Act in 1937 A.D. as a first commercial bank of Nepal with 10 million authorized capital.

Modern banking practices emerged with the establishment of Nepal Bank Limited in 1934 A.D. However the establishment of Nepal Bank Limited alone was not sufficient and satisfactory to conduct the banking activities in Nepal. As a result, "Nepal Rastra Bank" was established in 1956 A.D. as a central bank under Nepal Rastra Bank Act 1956 A.D. with an objective of supervision, protecting and directing the functions of commercial banking activities. Another commercial bank fully owned by the government named 'Rastriya Banijya Bank" was established in 1966 to spread banking services to both rural and urban areas. Similarly, "Agricultural Development Bank" was established in 1967 A.D. with an objective to develop and modernize agricultural sector.

After the restoration of democracy, the first elected government in 1991 adopted liberalized and market oriented economic policies followed by liberalization in the financial sector. These include the deregulation of interest rate, free entry of banks and financial institutions, removal of statutory liquidity ratio, formulation of new commercial banks, finance company and development banks act so as to encourage private sector including foreign banks and financial institutions. Since then, various financial institutions i.e. joint venture banks, domestic commercial banks, development banks, finance companies, co-operative banks, credit guarantee corporation, employee provided fund, national insurance corporation, Nepal stock exchange have come into existence to fulfill the financial needs of the country and assisting the financial development of the country.

Nepal Arab Bank Limited (NABIL) was the first joint venture bank established in 1984 A.D., which was joint venture with Dubai Bank Limited. Then two other joint venture banks Nepal Indosuez Bank Limited with joint venture of Grindlays Bank of London were established in 1986 A.D. but nowadays these banks name have been changed as Nepal Investment Bank Ltd. Respectively, Himalayan Bank Ltd. Joint venture with Habib Bank of Pakistan and SBI Bank Ltd. With State Bank of India were established in 1993 A.D. Everest Bank Ltd. Joint venturer with Punjab National Bank India (early it was joint ventured with United Bank of India Calcutta) and Nepal Bangladesh Bank Ltd. With SIAM

Commercial Bank Thailand was established in 1995 A.D. and Nepal Bank of Ceylon joint ventured with Ceylon Bank of Sri-Lanka was established in 1997 A.D. other several commercial banks like Lumbini bank, Siddhartha Bank, Marbal Bank, Suhrise BankAsian Bank, Prime Bank, Laxmi Bank and other development banks also established.

1.3 Introduction of Joint Venture Banks

The commercial bank firmed by joining two or more enterprises is known as joint venture bank. The main purpose of joint venture bank is to join economic forces in order to achieve desired goal. Joint venture banks are more efficient and effective monetary institution in modern banking field than other old types of bank in Nepalese context. The primary objective of the joint venture banks is always to earn profit by investing the loan to the people associate with trade, business, industry etc.

"Joint venture is joining of force between two or more enterprises for the purpose of carrying out a specific operation (industrial and commercial investment production or trade)" (Gupta, 1994: 15-24).

All the Nepalese JVBs are established and operated under the rules and regulations and guidance of Nepal Rastra Bank. Nepal Rastra Bank had issued a certain directive to those banks, regarding the mandatory credit accusation to the priority sector. Nepal Rastra Bankhas directed to the government owned banks to invest 3% and the JVBs to invest 0.50% of the total outstanding credit priority sector (Economic Report, 1997/98: 4).

Joint Venture Banks of Nepal

The history of joint venture banks is not so long. After establishment of democracy, the government adopted liberal and market oriented economic policy which facilitated the establishment and development of joint venture banks.

At present there are six joint venture banks in Nepal which are listed as follows:

S.N.	Name of Banks	Established Date	Head Office
1.	NABIL	2041/03/29	Kathmandu
2.	SCBNL	2043/10/16	Kathmandu
3.	HBL	2049/10/05	Kathmandu
4.	NBBL	2050/02/23	Kathmandu
5.	NSBIBL	2050/03/23	Kathmandu
6.	EBL	2051/07/01	Kathmandu

1.4 Profile of Concern Banks

A. Standard Chartered Bank Nepal Limited (SCBNL)

Standard Chartered Bank Limited was established in 1985 as a second foreign joint venture bank under the company act 1964 by the name of Nepal Grindlays Bank Limited. ANZ Grindlays Bank PIC held 50 percent of total capital and Nepali promoters held other half portion. Out of 50 percent, 33.34 percent shares are held by Nepal Bank Limited and remaining 16.66 percent shares by general public of Nepal. ANZ Grindlays Bank PLC is managing the bank under joint venture and technical service agreement singed between ANZ Grindlays Bank PLC and Nepali Promoters. Nepal Grindlays Bank Limited and changed its name as Standard Chartered Bank Limited (SCBNL). Its share subscription is given as:

ANZ Grindlays Bank PLC	-	50.00%
Nepal Bank Limited	-	33.34%
Nepalese Public	-	16.66%

The following extra facilities have been providing by the bank.

- Credit Cards
- Tele Banking
- Any Branch Banking
- ATM (Automatic Teller Machine)
- VISA Card
- 24 Hours Banking

The bank is also providing its banking facilities by establishing branches in different region and parts of the country, which includes both urban and rural areas.

The business hours of the bank are as follows:

Inside the Valley

Monday to Friday	-	09.30 AM to 03.00 PM (Transaction Hour)
	-	09.00 AM to 05.30 PM (Office Hour)

Outside the Valley

Sunday to Thursday	-	09.45 AM to 03.00 PM (Transaction Hour)
	-	09.00 AM to 05.15 PM (Office Hour)

(Friday it process for half of the day).

B. Nepal SBI Bank Limited (NSBIBL)

Nepal SBI Bank Limited (SBI) was established under the company act 1964, in 1993. This is the joint venture of state bank of India and Nepali promoters. The State Bank of India holds 50 percent shares of total investment. Nepal SBI Bank Limited is managed by the State Bank of India under the Joint Venture and Technical Services Agreement signed between it and Nepali promoters. Its share subscription is given as:

State Bank of India, India	-	50.00%
Employee Provident fund	-	15.00%
Agriculture Development Bank Ltd., Nepal (ADB/N)	-	05.00%
Nepalese Public	-	30.00%

The main objectives of the bank are to carryout modern banking business in the country under the commercial act 1974, and to provide loan on agriculture, commercial and industrial sectors.

The following facilities have been providing by the bank are :

- International Trade and Bank Guarantee
- Any Branch Banking
- Conventional Banking Facilities
- Remittances, etc.

The business hours of the bank are as follows:

<u>Inside the Valley</u>

Monday to Friday	-	09.30 AM to 03.00 PM (Transaction Hour)
	-	09.00 AM to 05.30 PM (Office Hour)

Outside the Valley

Sunday to Thursday - 09.45 AM to 03.00 PM (Transaction Hour)

- 09.00 AM to 05.15 PM (Office Hour)

(Friday it process for half of the day).

Profile of the other Commercial Banks

As of Mid-June 2008

Class A : Commercial Banks

S.N.	Name	Operation Date (A.D.)	Head Office	Paid up capital (Rs. in Lakhs)
1	Nepal Bank Ltd.	15/11/1937	Kathmandu	3804
2	Rastra Banijya Bank	23/01/1966	Kathmandu	11723
3	Agricultural Development Bank Ltd.	2/1/1968	Kathmandu	92780
4	Nabil Bank Ltd.	16/07/1984	Kathmandu	6892
5	Nepal Investment Bank Ltd.	27/02/1986	Kathmandu	12030
6	Himalayan Bank Ltd.	18/01/1993	Kathmandu	10135
7	Nepal Bangladesh Bank Ltd.	5/6/1993	Kathmandu	7441
8	Everest Bank Ltd.	18/10/1994	Kathmandu	8314
9	Bank of Kathmandu Ltd.	12/3/1995	Kathmandu	6031
10	Nepal Credit & Commerce Bank Ltd.	14/10/1996	Siddharthanagar, Rupend	12758
11	Lumbini Bank Ltd.	17/07/1996	Narayangadh, Chitwan	750
12	Nepal Industrial & Commercial Bank Ltd.	21/07/1998	Biratnagar, Morang	7920
13	Machhapuchchhre Bank Ltd.	3/10/2000	Pokhara, Kaski	8217
14	Kumari Bank Ltd.	3/4/2001	Kathmandu	9000
15	Laxmi Bank Ltd.	3/4/2001	Birgunj, Parsa	7320
16	Siddhartha Bank Ltd.	24/12/2002	Kathmandu	7900
17	Global Bank Ltd.	2/1/2007	Birgunj, Parsa	7000

18	Citizens Bank International Ltd.	21/06/2007	Kathmandu	5600
19	Prime Commercial Bank Ltd.	24/09/2007	Kathmandu	7000
20	Sunrise Bank Ltd.	12/10/2007	Kathmandu	7000
21	Bank of Asia Nepal Ltd.	12/10/2007	Kathmandu	7000
22	DCBL Bank Ltd.	23/01/2001	Kamaladi, Kathmandu	3010
23	NMB Bank Ltd.	26/11/1996	Babarmahal, Kathmandu	
24	Kist Bank Ltd.		Anamnagar Kathmandu	

1.5 Statement of the Problem

Various joint venture banks have been established to assist the process of economic development of our country. All joint venture commercial banks have played vital role in accepting deposits and providing various types of loans. Loan affects entire development of the country. The development of country is directly related to the volume of loan which also obtained from joint venture banks. The problem of lending has become very serious for developing country like Nepal. This is due to lack of sound investment policy of commercial banks.

J.V. Commercial banks are more confined to be making loan on short-term basis. They are less interested to invest on loan term projects because these banks are much more safety oriented. So they follow conservative loan policy which is based on strong security. The joint venture commercial banks seems to be indifferent to the national economic growth process. This is the main cause of crisis in the commercial banks and in the whole national economy as well.

The joint venture commercial banks have not formulated their investment policy in organized manner. They mainly rely upon the instructions and guidelines of Nepal Rastra Bank. They do not have clear view towards investment policy. Furthermore the implementation of policy has not been done in an effective way. Such banks invest their funds in limited areas to achieve higher amount of profit. This is regarded as very risky step, which may lead to lose in profit as well as principle. The investment done by joint venture banks to agriculture and industrial sector is not satisfactory to meet the needs of agriculture sector.

Except the joint venture banks there are other several financial institutions are being operated in Nepal. The fast growth of such organizations have made prorate increment in collecting deposits. They are not being able to find out new investments sectors required to mobilize their funds.

The interest rate structure in joint venture commercial banks is unorganized and unflavored resulted in higher spread rate, which discourages investments. Such banks have not paid attention towards proper matching of deposits and loan maturity, which has created several problems. Joint venture banks' investment has been found to have lower productivity, which is due to lack of supervision regarding whether there is proper utilization of their investment. Lack of farsihghtness in policy formulation and absence of strong commitment towards its proper implementation has caused merely problems.

Profit is must for a bank not only from the view point of bank but also from the view point of shareholders and depositors. And profit is only possible if the banks formulate proper and safe investment policy. Every bank must make profit to survive in the competitive market where there is a lot of money and very little investment opportunity exists. Therefore, appropriate investment policy is the fundamental function of all the joint venture commercial banks and other financial institutions.

The problems specially related to investment function of joint venture commercial banks presented briefly as under.

1. Utilization of available fund: Does the SCBNL utilize its avainance fund to it ? Appropriation in fund mobilization and investment policy. Is the SCBNL's fund mobilization and investment policy is effective and efficient than NSBIBL.

2. What is the relationship of investment and loan and advances with total deposit and total net profit of SCBNL and comparing its performance with NSBIBL ?

3. Does the investment decision affect the total earning of the bank ?

1.6 Objective of the Study

The specific objectives of the present research are to investigate investment practices and policies adopted by Standard Chartered Bank Nepal Ltd. and Nepal SBI Bank Ltd. in compare with each other. The specific objectives of the study are as follows:

1. To evaluate the liquidity management, asset management efficiency, profitability, risk position and investment practices of Standard Charted Bank Nepal Ltd. and Nepal SBI Bank Ltd.

2. To analyze the deposit and investment trends of the sample organization.

3. To recommend the policies to be adopted by the sample organization based the financial analysis for its future development.

1.7 Significance of the Study

The successful mobilization and utilization of domestic resources in must for any developing country to inspire a sustainable economic development. The joint venture banks have played vital role in the collection of scattered small savings from mass and converting them into meaningful investment. Deposit collection has no meaning, if it is not invested properly. Thus investment activity is the lifeblood of any financial institution as well as nation. Better return and sustainability are only possible through proper utilization of fund as investment. So, the investment practice is very important for the joint venture banks. The sound investment policy play vital role to earn good return from investment.

The comparative study on investment practice of joint venture banks would provide useful information to the management of concerned bank that would help them to take corrective action to improve the weaknesses to investment. Similarly, the concerned persons would get required information and can take the decision to make investment on shares of bank. In the same way the academic institution, bank employees, trainees and the others concerned with joint ventures bank would get useful feedback from this study.

1.8 Limitations of the Study

The basic limitations of this study are as follows:

1. This study is based on secondary as well as primary data.
2. Only the banks are taken for the study, which are Standard Chartered Nepal Bank Ltd. and Nepal SBI Bank Ltd.

3. The whole study covers the data of seven years of period.

4. Data, which are related to fund mobilization as loan and advance and investment in government securities and other financial institutions are considered.

5. Non availability of various references of source acts as constraints for the study.

1.9 Plan of the Study

This study has divided into five chapter's viz. introduction, review of literature, research methodology, data presentation and analysis and conclusion and recommendations.

First Chapter

This chapter deals with the introduction part of the study. It includes introduction of joint venture banks, background, history of the bank, statement of the problem, objective and significance of the study, plan of the study and limitations of the study.

Second Chapter

The second chapter deals with review of literature, which includes, review of books, review of bulletins, journals and annual reports published by banks and other related authorities, review of related articles and study of previous thesis as well.

Third Chapter

This chapter explains the research methodology used to evaluate investment practice of joint venture banks in Nepal. This chapter consists of research design, sources of data, population and sample, tools and methods of analysis.

Fourth Chapter

This chapter is analyzing chapter, which deals with presentation and analysis of data through definite course of research methodology. This chapter analyses different financial ratios and statistical analysis related to investment and fund mobilization of joint venture banks.

Fifth Chapter

This is the last chapter of the study, which provides summary and conclusion, suggestion and recommendations for overcoming the weaknesses and improving the future performance of the joint venture banks. Finally, an extensive bibliography and appendices are also presented at the thesis.

CHAPTER – II

REVIEW OF LITERATURE

2.1 Theoretical Frameworks

In this chapter, the focus has been made on the review of literature relevant to the investment practice of joint venture commercial banks. Then main purpose of review of literature is to find out what research studies have been conducted in one's chosen field of study and what remain to be done. Every study is very much based on past knowledge. The past knowledge provides foundation to the present study. This chapter helps to take adequate feedback to broaden the information and inputs to this study. This chapter has been divided into different parts, which have been arranged into the following order.

2.2 Meaning of Some Terminologies

i. Deposit

The sum of money collected by the banks from the depositors in different accounts is called deposit. The banks collect deposit from customers in various accounts like current account, saving account and fixed deposit account. Deposit is the main source of fund for the bank. Thus deposit is the lifeblood of the join venture commercial banks; the success of a bank greatly depends upon the extent to when it may attract more and more deposits. As deposits are borrowed amount from depositors, it is liability for the banks.

ii. Loan and Advances

Loan and advances is the main sources of income and most profitable assets to a bank. A bank is always willing to lend as possible since they constitute the larger part of revenue. A commercial bank hardly lends money for a long period. The commercial banks lend money for a short period of time that can be collected at a short period. The commercial banks never bounded to provide long-term loan because the banks have to synchronize the loans and advances with the nature of deposit they receive. The banks provide loan and advances against the personal security of the borrower or against the security of the immovable and movable properties. The banks provide loans in the various forms like overdraft, cash credit, direct, direct loan and discount bills of exchange.

iii. Investment in Government Securities, Shares and Debentures

Securities are the source of long term financing which involve shares and debenture issued by the government. The banks can extend credit by purchasing government securities i.e. share and debentures issued by government. However it is not major sources of income.

iv. Investment on other Company's Shares and Debentures

The joint ventures commercial banks also utilize their funds to purchase the shares and debentures of other companies. There are two motive behind investment of funds on other company's shares and debentures by the banks the first is to earn profit and the next is to meet the direct of Nepal Rastra Bank.

v. Assets

Every bank has its own assets. The resources or properties owned by the business are known as assets. Some examples of assets are cash, building, land, furniture, goodwill etc. such assets are owned by the banks to get current or future benefit.

vi. Liabilities

The amount or money payable by the banks to the outsiders within a certain period of time is known is liabilities of the bank. Liabilities are the financial obligation for the banks which must be met within a stated time. Liabilities should not be taken negatively as they are the sources of assets.

vii. Balance Sheet

Balance sheet is one of the important accounting statement which shows the true financial position i.e. position of assets and liabilities of organization. There are two side of balance sheet they are capital and liabilities and assets and properties sides. Thus balance sheet includes all assets, liabilities and capital.

viii. Retained Earning

It is the part of company profits which is not paid out in taxes or dividends, but is ploughed back into a business. Retained earning may be used to finance fixed investment to finance takeovers at other firms to increase liquid assets.

ix. Standard Deviation

The standard deviation is defined as the positive square root of the arithmetic mean of the squared deviation from their arithmetic mean of a set of values. It is also known as ***'Root Mean-Square Deviation'.*** It is denoted by ∃ (small sigma).

x. Coefficient of Variation (C.V.)

The relative measure based on the standard deviation is known as the coefficient of standard deviation by 100 is known as the coefficient of standard deviation. The coefficient based on standard deviation multiplied by 100 is known as coefficient of variation (C.V.) by the help of C.V. two distributions can be compared to find out their variability.

$$\text{C.V.} = \frac{\exists}{x\supseteq} \times 100$$

"Less the C.V. more will be the uniformly, consistency etc. and vice-versa."

xi. Arithmetic Mean

The sum of all the observations divided by the number of observations is called arithmetic mean (Pant and Chaudhary, 2053: 91).

xii. Correlation

Two variables are side to have 'correlation' when they are so related that change in the value of one variable make change in the value of other variable. Correlation analysis helps in determining the extent to which the two variables are correlated but it does not tell us about causes and effect relationship.

xiii. Ratio analysis

Ratio refers to the numerical or quantitative relationship between two items or variables. In simple language, ratio is one number expressed in terms of another and can be worked out by dividing a number with the other. So, it is calculated by dividing one item of the relationship with the other (Munankarmi, 2002: 468).

xiv. Off-Balance Sheet Activities

Off-balance sheet activities involve contacts for future purchase and sale of assets and all there activities are contingent obligations. These activities are not recognized as assets and liabilities on balance sheet. Some good examples of those are letter of credit (LC), Letter of Governance, Bills for Collection etc. These activities are very important, as they are the good sources of profit to the bank.

2.3 Features of Sound Lending and Investment Policy

The income and profit of the bank depends upon its lending procedures, lending policy and investments of its funds properly. The greater the investment made by the bank, the higher will be the profitability. A sound and effective investment policy is significant and crucial for the bank to earn higher profit and encourage proper saving for the developing and poor country like Nepal.

There are following some important features of sound lending and investment policy suggested by different authors, which the banks must consider.

i) Safety

A bank should be very much conscious and careful in investing procedures and sectors. The banks should never invest its funds on those securities, which are too much volatile because a small alter may cause great loss. The banks must invest funds in speculative businessman who may be bankrupt at once and who may earn million in a minute also. Similarly while making investment, bank should accept such type of security, which are durable, marketable and which has high market price.

ii. Stability of Income

Stability of income should also be considered while making investment. The banks should consider stability of monetary income and stability of purchasing power. However emphasis upon income stability may not always be constant with other investment principle.

iii. Profitability

Profit is essential for every bank for its survival and continuity. The banks should invest their funds in such sector from where maximum profit can be earned. The joint venture commercial banks can maximize its volume of wealth through maximization of return on their investment. The profit of joint venture commercial banks depends on the interest rate volume of investment and nature of investment in different securities.

iv. Liquidity

Liquidity generally refers to cash or any assets that can be converted into cash immediately. Similarly, liquidity refers to that state or position of a bank to meet all of its obligations. In other words, it refers to the capacity of the bank to pay cash against deposit. People deposit money at the ban k in different account with confidence that the bank will repay their deposit money when they need, to maintain such confidence of depositors, the bank must keep this point in mind while investing its funds in different securities or at the time of lending. So, that the banks can meet current or short-term obligations when become due for payment.

v) Legality

Illegal investment activities may cause problem to the investors. In the same way if the securities are issued illegally, it also may cause problem to the investors. Therefore all the joint venture commercial banks should operate the investing activities by following the directives of NRB, Ministry of Finance and other concerned authorities.

vi. Diversification

The banks should not grant he loan in only one sector. To minimize the risk a bank must diversify its investment on different sectors. Diversification of loan helps to sustain loss according to the law of average.

vii. Tangibility

A commercial bank should prefer tangible security to an intangible one. Though it may be considered that tangible properly does not yield on income a part from intangible security have lost their value due to due price level inflation.

2.4 Review of Legislative Provision

In this section, the review of legislative provision under which the commercial banks are operating has been discussed. This legislative environment has significant impact on the commercial banks establishments, mobilization of their banks have to confirm to the legislative provisions specified in the commercial bank act, 2031 and the rules and regulations formulated to facilitate the smooth running of commercial banks.

Policy Guidelines on Establishment of Commercial Banks

For the establishment of commercial banks, receiving application form had been stopped since 1995. Considering that such an administrative restriction is not in conformity with the liberal financial policy the following new policy guidelines have been made published on 16th May 2003.

i. About Paid up Capital

To establish new commercial banks for national level, paid up capital must be Rs. 1000 million, having its office in Kathmandu valley. Joint investment with foreign bank and financial institution or management contract at least for 3 years with such institutions is required. To establish the commercial banks in all the places in the kingdom other then in the Kathmandu valley, the paid up capital must be Rs. 250 million.

ii. About Share Capital

In general, the share of commercial banks will be available for the promoters 70% and general public 30%. The foreign banks and financial institutions could have a maximum of 67% share in investment on the commercial banks of national level. In order to provide adequate opportunity for investment to the Nepali promoters in national level banks, only 20% of total share capital will be made available to general public on the condition that the foreign bank and financial institutions are going to acquire 50% of the total share, in case of commercial banks to be established outside Kathmandu valley, shares investment of promoters and general public should stand at 70% and 30% respectively.

iii. Legal Procedure

Banks to be established with foreign promoter participation have also to be registered fulfilling all the legal processes prescribed by the prevalent Nepal laws.

iv. Banks already in Operation

Banks that is already in operation and those who have already acquired letter of intent before the enforcement of this provision have to bring their capital level with in seven years i.e. by 16th July, 2009, as per the recently declared provision. Such increase in the capital should be at a rate of 10% should be at the minimum.

v. Concerning up Graduation

Bank to be established outside Kathmandu valley could be aloud to operate thought out the kingdom including Kathmandu valley only on the condition that they have brought their paid up capital level to Rs. 1000 million and also fulfilled other prescribed conditions until and unless such banks do not get license to operate throughout the kingdom, they will not be allowed to open any office in Kathmandu valley.

vi. Promoters Share Payment Procedure

Of the total committed share capital, the promoters has to deposit in NRB an amount equal to 20% along with the application and another 30% at the time of receiving the letter of intent on a interest free basis.

The bank should put into operation with in one year of receiving the letter of intent. The promoters have to pay fully the remaining balance of committed total share capital before the banks comes into operation. Normally, within 4 months from the date of filling the application; NRB should give its decision for the establishment of the bank whether it is on favor against it. If it declines to issue license, it has to inform in writing with reasons to the concerned body.

viii. Promoters Qualification and Experience

Action on the application from promoters will not be initiated if it is proved that their collateral has been put on auction by the bank an financial institutions as a result of non payment of loans in the past, who have not cleared such loans or those in the bank list of the credit information bureau and 5 year have not elapsed from the date of removal of their name from such list. The application will be deemed automatically cancelled irrespective of it being on any stage of process for license issuance if the above events are proved, out of the total promoters, one-third should be its chartered accountant or at least a graduate of Tribhuvan University or recognized institutions with major in economics or accountancy, finance, law, banking or statistics. Likewise one-fourth promoters should have the work experience of bank of financial institution of similar nature.

viii. Promoters Share

Promoters group's share can be disposed or transferred only on the condition that the bank has been brought in operation, the share allotted t o the general public has been floated in the market and after completion of 3 years from the date it has registered in the stock exchange. But before the disposal of such shares it is mandatory to get approval from

NRB. The share allotted to general public has to be issued and sold within 3 years from the date the bank can not issue bonus shares or declare and distribute dividends, shareholders of the promoters from the same institutions.

ix. Branch Expansion

The commercial banks established in national level will initially be authorized to open a main branch office in Kathmandu valley. They will be authorized to open one more branch in Kathmandu valley only after they have opened two branches outside the Kathmandu valley.

x. Disqualify from Becoming Director

An individual who is already serving as a director in one of the bank of financial institutions licensed by NRB can not be considered eligible to become the director in other banks or financial institutions. Also, stock brokers, market makers and also an individuals and institution involved as an auditor of the bank and institutions carrying on financial transactions can not be a director (Economic Survey, 2002/03).

2.5 Directives Issued by NRB

The banks and financial institutions that are governed by BAFIA has to follow the rules and regulation as specified in the Act and also has to follow the directivities issued by NRB from time to time. On the basis of the authority given by BAFIA, NRB has issued directive from time to time as follows:

õ Capital Fund

The A, B and C class financial institutions are required to maintain minimum capital fund at the ratio of 6 percent and 12 percent of their core capital and capital fund respectively. But as for the D class financial institutions they are required to maintain capital fund at the ratio of 4 percent and 8 percent of their core capital and capital fund respectively.

õ **Loan Classification**

The loan of the licensed financial institution has been classified into the following heading: pass, substandard, doubtful and loss. Those loans that are not passed due or have passed due for a period up to three months come under the pass category, more than three months up to six months come under substandard category, more than six months up to one year come under doubtful category and past due for a period more than one year come under loss category.

õ **Loan Loss Provisioning**

The loan loss provision for the non-insured loan has to be made by the licensed financial institution at the rate of one percent for the loans that fall under pass category, 25 percent for substandard category, 50 percent that fall under doubtful category and 100 percent for loss category. In the case of insured loan the provision is 25 percent less than the noninsured loan. Accordingly, 0.25 percent for the loans that fall under for the pass category, 6.25 percent for substandard category, 12.50 percent for doubtful category and 25 percent loan loss provision for those non-banking assets acquired by the licensed financial institutions up to the FY 2002/03 which has not been disposed for a period of three years has to make provision for the FY 2003/04 at the rate of 33.33 percent, for FY 2004/05 at the rate of 66.67 percent and FY 2005/06 at the rate of 100.00 percent. In case of non-banking assets acquired during FY 2003/04 and there after, the provision for loss is 50 percent, 75 percent and 100 percent for the first, second and third year respectively.

- **Credit Limit**

The loan limit or A, B and C class licensed financial institution for the single borrower or the group of related borrower is 25 percent of the core capital and 50 percent of the non-fund based core capital fund. As for the D class licensed financial institution loan to the deprived and low income people can be extended up to the maximum limit of Rs. 60 thousand per group member or individual and Rs. 1.5 million to micro enterprise based on collateral.

- **Maintenance of CRR**

The CRR to be maintained in NRB by the A and B class licensed financial institution is 5 percent and as for the C class it is 2 percent of the total deposit liabilities. If the licensed financial institution fails to maintain the liquidity as to the directives then they have to pay penalty at the rate of existing bank rate for the first time, double the bank rate for the second time and for the third and successive times thereafter three times of the bank rate. As for the D class licensed financial institution the mandatory cash reserve to be maintained is 0.5 percent. Apart from the CRR this category of financial institutions is required to maintain the minimum liquidity ratio at 2.5 percent of deposit liability.

- **Branch Offices**

The A, B and C class licensed financial institutions are not allowed to open or close any of their branch offices without the prior approval of NRB. But in case of D class licensed financial institutions; the prior approval of NRB is not a prerequisite. The licensed institutions have to apply in NRB for opening a branch office and NRB will make the final approval only if the licensed institutions have fulfilled all the requirements for opening a branch.

- **Interest Rates**

The licensed financial institutions A, B and C class can fix their own interest rates on deposit as well as lending but the rates must be published in due time if there is change in the rates. In case of D class licensed financial institution, they can charge a fix rate of interest on loans and advances. But all the licensed financial institutions must inform all the changes to NRB within seven days of such changes. Further, the interest rate on loans and deposits of A, B and C class licensed financial institution must be published in the papers and as for the D class institutions, the rates may be published in the office board only.

- **Mobilization of Financial Resources**

The mobilization of financial resources for different class of licensed institution differs from one another. In case of A class there is no limitation, for B class it is 20 times of its core capital, for C class 15 times of their core capital and for D class 30 times of core capital. Deposit collection by A, B and C class licensed institution can collect institutional deposit only to the extent of 30 percent of total deposit for the FY 2005/06, 25 percent for the FY 2006/07 and there after it is fixed at 20 percent. But in case the deposit collected is more than the authorized limited then by FY 2005/06 or maturity period, the deposit has to be only up to the prescribed limit. As for borrowing, it depends upon the class and limit of the licensed institution as mentioned above.

2.6 Review of Relevant Studies

2.6.1 Receive of Books

Banks are such type of institution, which deal in money and substitute for money. They deal with credit and credit instrument. The important thing for the bank is good circulation of credit. Fluctuate flow of credit and weak decision harms the whole economy and the bank as well Good management of credit or credit instrument is very important for banks.

In the word of Gitman and Jochnk, "Investment is any vehicle into which funds can be placed with the expectation that will preserve or increase in value and generate positive return" (Gitman and Jochnk, 1990: 21).

"The secret of successful banking is to distribute resources between the various forms of assets in such a way as to get a sound balance between liquidity and profitability so that there is cash (on hand quickly realizable) to meet every claim and at the same time, enough income for the bank to pay its way and earn profit for its shareholders" (M. Radheswami/S.V Vasuderan, 1985: 219).

According to Chales P. Jones, "Investment is the commitment of funds to one or more assets that will be held over some future time period. Investment is concerned with the management of an investor's wealth, which is the sum of certain income and present value of all future income" (Jones, 1999: 33).

According to William. F. Sharpe, Gorden T. Alexander and Jeffery V. Baily, "Investment in it's broaden sense means the sacrifice of current dollars for future dollars. Two different attributes are generally involved : time and risk. The sacrifice takes place in the present and its magnitude is generally uncertain" (Sharpe, Alexander and Bail, 1998: 1).

In the words of Reed, Cotter, Gill and Smith, "Commercial banks still remain the heart of our financial system holding the deposits of millions of personal, governments and business units. They make funds available through their lending and investing activities to borrowers, individuals, business firms and governments. Commercial banks are the most important type of financial institutions in the nation in terms of aggregate assets" (Reed, Gill, Cotter and Smith, 1980: 5).

According to I.M. Pandey, "Investment decision expenditure and benefits should be measured in cash. In investment analysis, cash flow is more important than accounting profit. It may also be pointed out that investment decision affects the firm's value. The firm's value will increase if investments are profitable and add to the shareholder's wealth. Thus, investment should be evaluated on the basis of criteria, which is compatible with the objectives of the shareholder's fund maximization. An investment will add to the shareholder's wealth if it yields benefit in excess of the minimum benefits as per the opportunity cost of capital" (Pandey, 1999: 407).

"Investment has many factors. It may involve putting money into bonds, treasury bills or note or common stock or painting or real state or mortgage or oil venture or cattle or the theater. It may involve specially in bull markets or selling short in bear market. It may involve options, straddles, rights, warrants, convertibles, margin, gold silver, mutual funds, money market funds, index funds and result in accumulation wealth. Diversity and challenge characterize the field. For the able or lucky, the rewards may be uniformed results can be uniformed results can be disastrous (Ghone, Zinbarg and Zeiked, 1997: 1).

2.6.2 Review of Master's Degree and Ph.D. Thesis

Before this study, various students regarding various aspects of commercial banks and joint venture commercial banks such as investment policy, lending policy financial performance, interest rate structure etc., have conducted several thesis works. Some of them, as supposed to relevant for the study are presented below.

Mr. Raja Ram Khadka (1985) on his study, "A study on the investment policy of Nepal Arab Bank Ltd. (NBIL) compared NABIL with that of Nepal Grindlays Bank Ltd. (NGBL) and Nepal Indosuez Bank Ltd. (NIBL) the main objectives of the study were to evaluate the liquidity assets management efficiency and profitability positions in related to fund mobilization of NABIL in comparison to other joint venture banks (JVBs) with the objectives of :

- To evaluate the liquidity, assets management efficiency and profitability position in relation to fund mobilization of NABIL Bank Ltd. in the comparison of other joint venture banks.
- To discuss fund mobilization of NABIL Bank Ltd. in respect to its based off-balance sheet transactions and based on balance-sheet transactions in comparison of other joint venture banks (JVBs).
- To evaluate the growth ratio of loans and advances and total investment with respective growth rate of total deposit and net profit of NABIL Bank Ltd. in comparison to other JVBs.

- To find out the relationship between total deposit and total investment, total and total loan and advances, and net profit and outside assets of NABIL Bank in the comparison to other JVBs.

The findings of the study are as follows:

- The liquidity position of NABIL Bank Ltd. is comparatively worse than that of other JVBs. NABIL Bank has more portions of current assets as loans and advances but less portion of investment on government securities.
- NABIL Bank is comparatively less successful in on-balance-sheet operation as well as off-balance sheet operation than that of other JVBs.
- There is significant relationship between deposit and loan advances as well as outside assets and net profit but not between deposit and total investment in case of both NABIL Bank Ltd. and other JVBs.
- Profitability position of NABIL Bank Ltd. is not better than that of other JVBs.
- NABIL Bank is more successful in deposit mobilization but failure to mountain high growth rate of profit in comparison to other JVBs (Khadka, 1998).

Mr. Upendra Tuladhar (1988) has conducted a study on, "A study on investment policy of Nepal Grindlays Bank Ltd. in the comparison to other joint venture banks of Nepal" with the following objectives.

- To study the fund mobilization and investment policy with respect to fee-based off-balance sheet transactions.

- To evaluate the growth ratios of loan and advances and investment with respective growth rate of total deposit and net profit.

- To study the liquidity, efficiency of assets management and profitability position.

- To perform an empirical study of the customer's views and ideas regarding the existing services and adopted investment policy of the joint venture banks.

From his study following conclusions were drawn:

- Nepal Grindlays Bank Ltd. (NGBL) has maintained consistent and successful liquidity than NABIL Abk and Himalayan Bank Ltd. (HBL).

- The mean of total investment to total deposit ratio of Nepal Grindlays Bank Ltd. is higher than the other JVBs. The mean of the loan and advance to total deposit ratio of Nepal Grindlays Bank Ltd. is less and inconsistent than NABIL and HBL.

- Loan and advances to working fund ratio of other banks. Investment on government securities to working fund ratio of NGBI had the highest mean ratio than NABIL Bank Ltd. and Himalayan Bank Ltd. during the study period.

- It was found that total off-balance sheet operation to loan and advance ratio of NGBL is found to be the higher mean ratio than that of NABIL and HBL. It means NGBL used to perform the highest off-balance sheet operation than NABIL and HBL i.e. used to give priority to provide letter of credit, guarantee and others (e.g. trade finance) excessively than to others.

- The profitability position of NGBL is higher than NABIL Bank and HBL as well as it used provide interest to the customers for different activities consistently.
- The volume of growth ratio of loan and advances of NGBL is found higher than that of NABIL Bank Ltd. and lower than HBL. It indicates that all the JVBs used to provide loan and advances in increasing manner.
- The higher ratio of net profit of NGBL seemed to be more satisfactory than NABIL Bank Ltd. but in case of HBL it seemed to be very high (Tuladhar, 2000).

Dr. Sunity Shrestha (1993) has conducted a study on "Investment planning of commercial Banks in Nepal" with the following objectives:

- To evaluate the investment of commercial banks of Nepal with reference to securities, loans and advances.
- To establish the relationship of bank portfolio variables with the national income and interest rates.

The research was conducted on the basis of primary and secondary data of commercial banks.

The research findings of the study are summarized as follows:

- The general trend of commercial banks assets holding is growing. Deposits have been major sources of funds. The excess reserve level of the banks allows idle money and loss of opportunity. Debt equity ratios are very high, greater than 1005.

- The return ratios are on the average higher for foreign joint venture banks than for the Nepalese banks.

- The hypothesis that the commercial banks have non-professional style of decision making in investment has been accepted. The investment of commercial banks in shares and securities is normal and not found to have strategic decision towards investment in shares and securities.

- Investment in various sectors has a positive impact on the national income from their respective sectors.

- Investment in various economic sectors shows industrial and commercial sector taking higher share of national income from their respective sectors.

- Lending in priority sectors showed cottage and small industry sector sharing higher loans (Shrestha, 1993).

Prem Bahadur Shahi (1999) conducted a study on "Investment policy of commercial banks in Nepal" with the main objectives of :

- To evaluate the liquidity, asset management efficiency and the profitability and risk position of Nepal Bank Limited to the joint venture banks.

- To discuss fund mobilization and investment policy of Nepal Bank Limited in respect to its fee based off-balance sheet transaction and fund based on-balance sheet transaction in comparison to the joint venture banks.

- To find out the empirical relationship between various important variables i.e., deposits, loan and advances, investment, net profit, etc.

- To analyze the deposit utilization trend and its projection for nest five years of the Nepal Bank Limited and compare it with that of the joint venture banks.

- To provide a package of workable suggestions and possible guidelines to improve investment policy of Nepal Bank Limited and the joint venture banks based on the finding of the analysis, for the improvement of financial performance of Nepal Bank Limited in future.

The research was conducted mainly on the basis of the secondary data. The research findings of the study are as follows:

- The liquidity position of Nepal Bank Limited is comparatively better than that of the JVBs. Highly fluctuating liquidity position shows that the bank has not formulated any stable policy. It can also be conducted that Nepal Bank Limited has more portions of current assets as loan and advances but less portion as investment on government securities.

- The mean ratio of loan and advances to total deposit of Nepal Bank Limited is slightly lower than that of the JVBs. The mean ratio of total investment to total deposit of Nepal Bank Limited is lower than that of the JVBs. The mean ratio of investment on government securities to total working fund of Nepal Bank Limited is slightly lower than that of the JVBs. The mean ratio of total off-balance sheet operation to loan and advances of Nepal Bank Limited if found significantly lower than that of JVBs. So it was concluded that Nepal Bank Limited is comparatively less successful in on-balance sheet s well as off-balance sheet operations than that of the JVBs. It has not followed any definite policy with regard to the management of its assets.

- Profitability position of Nepal Bank Limited is comparatively not better than that of the JVBs. It indicates that Nepal Bank Limited must maintain its high profit margin in future.

- There is comparatively higher risk in Nepal Bank Limited than that of the JVBs regarding various aspects of the banking function.

- From the analysis of different growth ratios it can be concluded that Nepal Bank Limited has not been more successful to increase its sources of funds i.e., deposits and mobilization of it, i.e. loan and advances and total investment. Similarly, it seems to have failed to maintain high growth rate of profit in comparison to that of other JVBs.

- It has been found that there is significant relationship between deposits and loan and advances. There is negative relationship between deposits and investment in case of Nepal Bank Limited and positive in case of the JVBs.

- Nepal Bank Limited has higher trend analysis values of loan and advances and deposit, but lower trend values of net profit and total investment in comparison to the JVBs for next 5 years.

- Highly fluctuating ratios of Nepal Bank Limited show that it has not formulated any stable policy to maintain its liquidity in a consistent manner.

High portion of cash and bank balance in Nepal Bank Limited shows its negligence and inefficiency in its best utilization. It has not considered the cost of fund and its opportunity costs.

Higher percentage of loan loss relations shows that Nepal Bank Limited is weak in credit collection. There is absence of a sound credit collection policy. Nepal Bank Limited has not followed innovative appraisal, improper collateral evaluation, irregular supervision, etc. is a severe problem for the bank's success (Shahi, 1999).

Mr. Lila Prasad Ojha (2002) conducted a study on "Lending Practices: A Study of NABIL Bank Ltd., Standard Chartered Bank Nepal Ltd. and Himalayan Bank Ltd." with the objective of :

- To determine the liquidity position, the impact of deposit in liquidity and its effect on lending practices.
- To measure the bank's lending strength.
- To analyze the portfolio behavior of lending and measuring the ration and volume of loans and advances made in agriculture, priority and productive sector.
- To measure the lending performances in quality, efficiency and it contribution in total income.

The study was conducted on the basis of secondary data.

The research findings of the study are :

- The measurement of liquidity has revealed that the mean current ratio of all the three banks is not widely varied. All of them are capable in discharging their current liability by current asset.

- The measurement of lending strength in relative terms has revealed that the total liability to total assets of SCBNL has the highest ratio. the high ratio is the result of high volume of shareholder equality in the liability mix. Himalayan Bank Ltd. has high volume of saving and fixed deposits as compared to current deposit resulting into low ratio of non-interest bearing deposits to total deposits ratio compared to the combined mean.

- Grindlays Bank Ltd. used to perform highest off-balance sheet operation than the other two JVBs i.e., used to give priority to provide letter of credit, guarantee and others (e.g. trade finance) excessively than to others.

- The mean of investment on shares and debentures to total working fund ration of Nepal Grindlayts Bank Ltd. was found less than NABIL Bank Ltd. but higher than Himalayan Bank Ltd.

- The profitability position of Nepal Grindlays Bank Ltd. is higher than NABIL Bank Ltd. and Himalayan Bank Ltd. as well as it use to provide interest to the customers for different activities consistently.

- The volume of growth ratio of loan and advances of Nepal Grindlays Bank Ltd. is found higher than that of NABIL Bank Ltd. but lower than Himalayan Bank Ltd. It indicates that all the JVBs used to provide loan and advances in increasing manner.

- From the analysis of growth ratio of total investment it is found that Nepal Grindlays Bank Ltd. and NABIL Bank Ltd. have negative growth ratio i.e., they used to reduce the investment during the study period. But it is increasing in the case of Himalayan Bank Ltd.

- The growth ratio of net profit of Nepal Grndlays Bank Ltd. seemed to be more satisfactory than NABIL Bank Ltd. but increase of Himalayan Bank Ltd. it seemed to be very high (Ojha, 2002).

Mr. Akur Acharaya (2007) has conducted a study on "Investment policy analysis of commercial bank: a comparative study of NIBL with EBL and NABIL bank will the following objectives:

- To evaluate the liquidity, profitability, risk position and assets management of the sample banks.

- To evaluate and discuss the investment policy and fund mobilization of NIBL, EBL and NABIL.

- To show the relationship between deposit and investment trends of the bank.

Conclusion from his study:

- Liquidity position of NIBL is comparatively average than NABIL and EBL.

- Assets management ratio of NIBL occupy the average position in comparison with other two banks NABIL and EBL.

- NIBL is successful in utilization its overall working fund on profit generating activity than the NABIL and EBL. But return from loan and advances ratio is comparatively average, in this EBL has taken best position.

- From the study of capital risk ratio and credit risk ratio of all three banks comparatively NIBL is successful to attract the deposits and inter banks fund, and utilize its loan and advances form total assets in safest way by taking high risk, which helps to increase the level of profit and maximizing the value of the firm.

2.6.3 Review of Articles and Research Paper

Mr. Sunil Chopra in his article, "Role of Foreign Banks in Nepal" had written that the joint venture banks playing an increasingly dynamic and vital role in the economic development of the country that will undoubtly increase with time.

Mr. Bodhi B. Bajracharya, in his article entitled, "Monetary Policy and Deposit Mobilization in Nepal" has concluded that the mobilization of domestic saving is one of the monetary policies in Nepal. For this purpose commercial banks stood as the vital and active financial intermediary for generating resources in the form of deposit of the private sector for providing credit to the investor's in different sector for providing credit to the investor's in different aspects of economy" (Bajracharya, 2047: 93-97).

Bhaskar Sharma in his article "Banking the Future Competition" has mentioned that-due to the lack of investment avenues, banks are tempted to invest without proper credit appraisal and one personal guarantee, whose negative side effect would show colors only after 4 or 5 yeas; again he mentioned that private commercial banks are have been mushroomed only in urban areas where banking transaction in large volume is possible. The rural and suburban areas mostly remain unattended too. This is likely to prevail till completion takes its full rein in the urban areas" (Sharma, 2002: 13).

Mr. Shekhar Bahadur Pradhan, in his article "Deposit Mobilization, its problem and prospects" has presented that deposit is the life blood of every financial institutions, be it commercial bank, finance company co-operative or non government organization. He further adds in consideration of most of banks and finance company, the latest figure does produce a strong feeling that a serious review must be made of problems and prospects of deposit sectors. Leaving few joint ventures banks, other organizations rely nearly on the business deposit and credit disbursement.

Mr. Pradhan has highlighted following problems of deposit mobilization in Nepalese context.

1. Most of the Nepalese people do not go for saving in institutional manner due to the lack of good knowledge. Their reluctance to deal with institutional system is generated by the lower level of understanding about financial organization process, withdrawn system, and availability of depositing facilities and so on.

2. Unavailability of the institutional services in rural areas.

3. Due to lesser office house of banking system people prefer holding the cash in the personal possession.

4. No more mobilization and improvement of the employment of deposits and the loan sectors.

Mr. Pradhan has also recommended for the prosperity of deposit mobilization which are as follows:

1. By providing sufficient institutional in the rural areas.
2. By cultivating the habit of using rural banking unit.
3. By adding service hour system to bank.
4. Nepal Rastra Bank should also organize training program to develop skilled manpower.
5. By spreading co-operatives to the rural areas to develop mini branch services (Pradhan, 2053: 13).

Sunity Shrestha in her article "Financial Performance of Commercial Banks" has analyzed the following points.

1. The structural ratio of commercial banks shows that banks invest on the average 75% of their total deposit on the government securities and the shares.
2. Return ratio of all the banks shows that most of the time the foreign banks have higher return as well higher risk then Nepalese banks.
3. The debt ratios of commercial banks are more than 100% in most of the time period under study period. It leads to conclude that the commercial banks are highly leveraged and highly risky.
4. The foreign banks have comparatively higher total management achievement index (Shrestha, 1997: 23-27).

According to a report published in the magazine the Boss.

The financial sector has evolved as the biggest sector in the economy. There are altogether 128 financial institutions (excluding Nepal Rastra Bank, micro financial institutions and cooperative registered with cooperative board) in the country and currently more than 20,000 people employed in this sector. This human resources is responsible for managing approximately NPR 221 bn worth of assets (primarily loans and advances) out of which 50% comprises of two large banks of Rastriya Banijya Bank and Nepal Bank Ltd. annual net profit of NPR 5.89 be generated by creating assets worth of NPR 221 be last year means a very low return on assets (mere 2.21 percent, which is even below the average savings deposit in the country.

While doing root cause analysis for this scenario two very strong reasons have evolved. The first reason is the poor quality of loans, more particularly in government-owned banks and some private banks, due to non-compliance of basic credit principles while granting loans coupled with lack of credit-skills assessment. The second reason for lower return can be attributed to the fact that almost all the financial institutions are involved only in dealing wit undifferentiated vanilla banking products (The Boos, October, 2006: 75).

CHAPTER – III

RESEARCH METHODOLOGY

3.1 Introduction

In the last two chapters, general background of joint venture banks has been highlighted and review of literature with possible review of relevant books, articles, thesis, and research findings has also been discussed. This has equipped me with the inputs necessary for my study and helped me to make choice of research methodology to support my study in realistic terms with sound empirical analysis.

Research methodology is the way to solve the research problem systematically, which includes many tools and techniques, which is necessary for ever study. "Research Methodology refers to the thesis studying a problem with certain objectives in view. In other words, research methodology describes the methods and process applied in the entire subject of he study" (Kothari, 1989: 3).

The concise Oxford Dictionary defines research as "A systematic investigation into and study of materials source etc. in order to establish facts and reach new conclusion."

3.2 Research Design

"A research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure" (Kothari, 1989: 3).

Research design basically involves the following:

- Clarified data collection method.
- Defines the measurement approach.
- Defines the object to be measured.
- Clearly defines the way in which the data are to be analyzed.

In this way, research design is the plan, structure and strategy of investigations conceive to control variances. It is arrangement of conditions for collection and analysis of data. It is also on outline of the scheme to be used to gather and analyze the data. To achieve objective of this study, descriptive and analytical research design has been used.

Several financial and statistical tools have been applied to examine facts and descriptive, techniques have been adopted to evaluate investment practice of joint venture banks.

3.3 Population and Sample

There are total 25 commercial banks in Nepal listed in Nepal stock exchange. Out of these banks only the joint venture banks vez. SCBNL, NSBI have been selected for research and their data related to investment practice are comparatively studied.

3.4 Nature and Sources of Data

The study is based on primary and secondary data. The data and information have been collected from different sources. The sources of data and information used in this study are as follows:

- Annual reports
- Authorized websites
- Previous research, Thesis and case studies
- Journals and Articles

- Related Books
- Primary data has also been used especially questionnaire which is written in details in Annex.

Primary data is a data which has not been used by others. Collected fresh data is primary data. It can be prepared by different sources like opinion poll, sampling, through correspondents etc. (Sharma, 2003: 17).

In this study, primary data has been collected by using questionnaire method, for this interview and structured questionnaire method have been used. Nine questions were asked to the executive level staff of the related bank. The questions raised are of three types; yes/no question, multiple choice questions (close end) and open end questions.

Secondary sources refer to those for already gathered by others. The sources of secondary data can be divided into two groups: Internal and External. The internal secondary data are found within the company. Sources of such data include sales information, accounting data and internally generated reports. External secondary data are collected from sources outside the company. Such sources may include books, periodicals, published reports, data services, and computer data bank (Wolf and Pant, 2004: 194).

3.5 Method of Analysis

To achieve the objectives of the study, various financial, statistical and accounting tools have been used in this study. The analysis of data will be done according to pattern of data available. Because of limited time and resources, simple analytical statistical tools such as graph, percentage, Karl Pearson's Coefficient of Correlation and the method of least square have been adopted in this study. Similarly some financial tools such as ratio analysis and trend analysis have also been used for financial analysis.

The various calculated result obtained through financial, accounting an statistical tools are tabulated under different heading. Then, they are compared with each other to interpret the result. The tools are as follows:

3.5.1 Financial Tools

Financial tools help to identify and analyze the financial strength and weakness of the organization presenting the relationship between the item of balance sheet. For the purpose of this study, ratio analysis has been mainly used and with the help of it, data have been analyzed.

Ratio analysis is a technique of analysis and interpretation of financial statement through mathematical expression. It may be defined as mathematical expression of the relationship between two accounting figures. To evaluate the different performances of an organization by creating the ratios from the figures of different accounts is termed as ratio analysis. In short, ratio analysis can be defined as an analysis of financial statement with the help of ratios.

A. Liquidity Ratio

Liquidity ratio measures the ability of the firm to meet current obligations. It reflects the short-term financial strength of the business.

i. Cash and Bank Balance to Total Deposit Ratio

Cash and bank balance are the most liquid current assets of a firm, cash and bank balance to total deposit ratio measures the percentage of most liquid assets to pay depositors immediately. Cash and bank balance includes cash on hand, foreign cash on hand, cheques and other cash items balance with bank. The total deposit consists of current deposits, saving deposits, fixed deposits, money at call and short notice and other deposits. This ratio computed by dividing cash and bank balance by total deposit. This can be stated as :

$$\text{Cash and Bank Balance to Total Deposit Ratio} = \frac{\text{Cash and Bank Balance}}{\text{Total Deposit}}$$

ii. Cash and Bank Balance to Current Assets Ratio

This ratio measures the percentage of liquid assets i.e. cash and bank balance among the current assets of a firm. Higher ratio shows the higher capacity of firms to meet the cash demand. This ratio be stated as follows:

$$\text{Cash and Bank Balance the Current Assets Ratio} = \frac{\text{Cash and Bank Balance}}{\text{Current Assets}}$$

iii. Investment on Government Securities to Current Assets

This ratio used to find the percentage of current assets invested in government securities, treasury bills and development bonds. This ratio can be calculated by dividing the amount of investment on government securities by the total amount of current. It can be stated as follows:

$$\text{Investment on Govt. Securities to Current Assets Ratio} = \frac{\text{Investment of Govt. Assets}}{\text{Current Assets}}$$

iv. Loan and Advance to Current Assets Ratio

Loan is major earning source of bank. Lion are also taken as current assets as most of them are matured within a period of one year and represent short-term disbursement. A bank should not allocate all funds in loan and advances to total current assets, this is obtained by dividing loan and advances by current assets.

$$\text{Loan and advance to current assets ratio} = \frac{\text{Total Loan and Advance}}{\text{Total Current Assets}}$$

B. Assets Management Ratios (Activity Ratios)

Assets management or activity ratios are used to evaluate the efficiency with which the firm manages and utilize their available resources. The following ratios are used under assets management ratio.

i) Total Investment to Total Deposit Ratio

This ratio indicates how properly firms' deposits have been invested on government securities, on debenture and bonds, and on shares debentures of other companies. This ratio can be calculated by dividing total amount of investment by total amount of deposit collection. It can be stated as following:

$$\text{Total Investment Total Deposit Ratio} = \frac{\text{Total Investment}}{\text{Total Deposit}}$$

ii) Loan and Advances to Total Deposit Ratio

This ratio is used to find out how successfully the banks and finance companies are utilizing their total collections/deposits on loan and advances for the purpose of earning profit. It can be stated as:

$$\text{Loan and Advance to Total Deposit Ratio} = \frac{\text{Total Loan and Advance}}{\text{Total Deposit}}$$

iii) Loan and Advance to Total working Found Ratio

This ratio indicates the ability of banks and finance companies in terms of earning high profit from loan and advances. Total amount of assets given on balance sheet which refers to current assets, net fixed assets, loans for development banks and other miscellaneous assets but excludes off-balance sheet items like letter of credit, letter of guarantee etc. This ratio can be states as:

$$\text{Loan and Advance to Total Working Found Ratio} = \frac{\text{Loan and Advance}}{\text{Total Working Fund}}$$

iv) Investment of Government Securities to Working Fund Ratio

Investment of government securities to working fund ratio indicates how much part of total investment is there on government securities in percentage. It can be stated as:

$$\text{Investment of Government securities to working fund ratio} = \frac{\text{Investment in Govt. Securities}}{\text{Total Working Fund}}$$

v) Investment on Shares and Debentures to Total Working fund Ratio

This ratio shows the investment of Banks and Finance companies on the shares and debentures of other companies. It can be calculated by dividing investment on shares and debentures by total working fund. This can be stated as:

$$\text{Inv. on Shares and Debentures to Total Working Fund Ratio} = \frac{\text{Inv. on Shares and Debentures}}{\text{Total Working Fund}}$$

C. Profitability Ratios

Profitability ratios are very important to measure the overall efficiency of operations of 'firm'. It is true indictor of the financial performance of each and every business organization. The following ratios are taken under this heading.

i) Return on Total Working Fund Ratio

This ratio establishes the relationship between net profit and total working fund. The net profit indicates the part of income left to the internal equities after all costs charges, expenses have been deducted. It can be stated as :

$$\text{Return on Total Working Fund Ratio} = \frac{\text{Net Profit}}{\text{Total Working Fund}}$$

ii) Total Interest Earned to Total Working Fund Ratio

This ratio shows the relationship between total interest earned and total working fund. This ratio measures the percentage of total to assets A high ratio indicates the better performance of the bank. This ratio is calculated by dividing total interest earned from investment by total working fund. It can be stated as :

$$\text{Fund Ratio} = \frac{\text{Total Interest Earned}}{\text{Total Working Fund}}$$

iii. Total Interest Paid to Total Working Fund Ratio

This ratio measures the percentage of total interest expenses against total working fund. A ratio indicates higher interest expenses on total working fund and vice-versa. This ratio is calculated by dividing total interest paid by total working fund. It can be stated as :

$$\text{Total Interest Paid to Total Working Fund Ratio} = \frac{\text{Total Interest Paid}}{\text{Total Working Fund}}$$

iv) Return on Loan and Advance Ratio

Return on Loan and Advance Ratio shows how efficiently the banks and finance companies have utilized their resources to earn good return by providing loan and advances. This ratio is computed by dividing net profit/loss by total amount of loan and advances. It can be stated as :

$$\text{Return on Loan and Advance Ratio} = \frac{\text{Net Profit/Loss}}{\text{Total Loan and Advance}}$$

D. Risk Ratios

Risk taking is the prime factor of business transaction of investment management. If a firm bears risk, it increases the effectiveness and profitability of them. These ratios indicate the amount of risk associated with various financial operations.

The following ratios are used under this topic to :

i. Credit Risk Ratio

This ratio helps to measure the possibility of loan non repayment or the possibility of loan to go into default. Such ratio is calculated in percentage by dividing total loan and advances by total assets. It can be stated as :

$$\text{Credit Risk Ratio} = \frac{\text{Total Loan and Advances}}{\text{Total Assets}}$$

ii. Liquidity Risk Ratio

The cash and bank balance are the most liquid assets and they are considered as banks liquidity source and deposit as the liquidity needs. Cash and bank balance to total deposit ratio is indicator of bank's liquidity need. This ratio is low if funds are kept idle as cash and bank balance but this reduces profitability when the banks provide loan its profitability as well as risk increases. In this way, higher liquidity ratio indicates less profitable return and vice-versa. This ratio is calculated by dividing cash and bank balance to total deposit. It can be stated as:

$$\text{Liquidity Risk Ratio} = \frac{\text{Total Cash and Bank Balance}}{\text{Total Deposit}}$$

E. Growth Ratio

This ratio indicates how properly the banks are maintained their economic and financial condition. Growth ratios are related to fund mobilization and investment management of bank. Higher ratios represent the better performance of selected banks. Following growth ratios are calculated under this :

i. Growth Ratio of Total Deposit
ii. Growth Ratio of Total Investment
iii. Growth Ratio of Net Profit
iv. Growth Ratio of Loan and Advance

3.5.2 Statistical Tools

Some important statistical tools have been used to achieve the objectives of this study. They are as follows:

i. Arithmetic Mean (A.M.)

ii. Standard Deviation (S.D.)

iii. Coefficient and Regression (C.V.)

iv. Correlation and Regression Analysis and Probable Error (P.E.)

v. Trend Analysis

vi. Test of Hypothesis

i. Arithmetic Mean (A.M.)

The sum of all the observations divided by the number of observations is called arithmetic mean. The arithmetic mean is usually denoted by ($x\supseteq$). It is calculated by using the following formula.

$$x\supseteq = \frac{x}{n}$$

Where,

X = The sum of observations

n = no. of observations

ii. Standard Deviation (S.D.)

The standard deviation is defined as the positive square root of the arithmetic mean of the square deviation from their arithmetic mean of a set of values. It is denoted by the Greek letter 6 (small sigma) A small standard deviation means a high degree of uniformity of the observations as well as homogeneity of a serious, a large standard deviation means just opposite. It is calculated by using the following formula.

$$\text{S.D. } (\exists) = \sqrt{\frac{1}{N}(\ x - x\supseteq)^2}$$

Where,

N = Number of observations

X = Expected return of the historical data

iii. Coefficient and Regression (C.V.)

The coefficient of variation is the most commonly used measure of relative variation. It is used in such problems where the researcher wants to compare the variability of more than two years. A distribution having less C.V. is said to be less variable or more homogenous or more equitable than other. A distribution having greater C.V. is said to be more variable of more heterogeneous or less consistent of less uniform of less stable or less equitable than other. It can be calculated as following formula.

$$C.V. = \frac{\exists\ (S.D.)}{x\supseteq} \times 100$$

iv. Correlation and Regression Analysis and Probable Error (P.E.)

This statistical tool is used to analyze, identify and interpret the relationship between two or more variable. It interprets the relationship between two or more variable are correlated positively or negatively. This statistical tool helps to take several decisions.

For the purpose of decision making interpretation is based on following term.

- When r = 1, there is perfect positive correlation.
- When r = 1, there is perfect negative correlation.
- When 'r' lies between 0.7 to 0.999 (-0.7 to 0.999), there is high degree of positive (or negative) correlation.
- When r lies between 0.5 to 0.699 there is moderate degree of correlation.

- When r is less than 0.5, there is low degree of correlation.

Following formula is used to calculate Karl Pearson's coefficient of correlation.

$$r = \frac{(x - x\supseteq) \times \quad (y - y\supseteq)}{\sqrt{\quad (x - x\supseteq)^2 \times \quad (y - y\supseteq)^2}}$$

Where,

$(x - x\supseteq)$ = Sum of observation in series X

$(y - y\supseteq)$ = Sum of observation in series Y

$(x - x\supseteq)^2$ = Sum of square observation in series X

$(y - y\supseteq)^2$ = Sum of square observation in series Y

Karl Pearson's coefficient of correlation has been used to find out the relationship between the following variables

a. Coefficient of correlation between loan and advances and net profit.
b. Coefficient of correlation between deposit and loan and advances.
c. Coefficient of correlation between deposit ant total investment.

v. Probable Error (P.E.)

Probable error is used to measure for testing the reliability of an observed value of correlation coefficient. It is computed to find out the extent to which it is dependable. If coefficient of correlation is greater than 6 times of probable error, the observed value of r is said to be significant, otherwise nothing can be concluded with certainty. It is calculated by using following formula :

$$P.E. = 0.6745 \times \frac{1 - r^2}{\sqrt{n}}$$

Where,

r = Coefficient of correlation

n = Number of observations

vi. Trend Analysis

Trend analysis is statistical tool which compares financial ratios over a period of time. it gives an indication of the direction of change and reflects whether the firm's financial performance has improved, deteriorated or remain constant over time. This statistical tool has been used to interpret the trend of deposits, loan and advance, investments and net profit of banks from.

The future trend is forecasted by using the following formula :

$y_c = a + bx$

Where,

y_c = The dependent variable

a = Arithmetic mean

b =

x = The independent variable

vi. Test of Hypothesis

Under these analyses the effort has been made to test the significance level regarding the parameter of the population on the sample drawn from the population. The following steps have been followed for the test of hypothesis.

- Formulating hypothesis (Null hypothesis and Alternative hypothesis)
- Computing the test statistics.

- Fixing the level of significance.
- Decision making.